to future payments if the income produced by certain assets was less than an agreed upon amount. On December 1, 1991, an agreement was executed in which Y relinquished its rights to Federal financial assistance under the September 10, 1988 agreement in return for a lump sum payment. The lump sum payment represented a prepayment of the principal and accrued but unpaid interest for the note, and the rights to the contingent future loss and income payments. The entire prepayment is excluded from the income of Y because it is a prepayment of Federal financial assistance and the assistance (i) would have been provided pursuant to an acquisition that occurred before May 10, 1989, would have been provided pursuant to an assistance agreement executed before May 10, 1989, and would, if it had been provided prior to May 10, 1989, have been governed by a pre-FIRREA version of section 597; and (ii) the prepayment is paid to a party to the assistance agreement.

Example 2. The facts are the same as those in *Example 1,* except that the note bears an above market rate of interest and part of the lump sum represents a premium payment for the note. The portion of the lump sum allocable to the premium payment is also excluded from the income of Y because the payment represents the present value of the right to future Federal financial assistance in the form of interest.

Example 3. The facts are the same as those in *Example 1,* except that a portion of the lump sum payment represents compensation for additional expenses Y may incur in the future because of termination of the September 10, 1988 agreement. The portion of the lump sum payment allocable to the compensation for additional expenses must be included in the income of Y because it is not a prepayment of Federal financial assistance provided for by a written agreement entered into prior to May 10, 1989.

Example 4. The facts are the same as those in *Example 1,* except that instead of a new assistance agreement, the September 10, 1988 assistance agreement was modified on December 1, 1991. The modified agreement provided new Federal financial assistance in addition to the amounts previously agreed to. None of the new Federal financial assistance is governed by this regulation because the new assistance was not provided for by a written agreement entered into prior to May 10, 1989. The modification does not, however, affect the tax treatment of assistance provided for by the agreement prior to its modification.

(e) *Effective Date.* This section is effective April 23, 1992 for assistance received or accrued on or after May 10, 1989 in connection with acquisitions before that date.

[T.D. 8406, 57 FR 14795, Apr. 23, 1992. Redesignated and amended by T.D. 8471, 58 FR 18149, Apr. 8, 1993]

BANK AFFILIATES

§ 1.601–1 Special deduction for bank affiliates.

(a) The special deduction described in section 601 is allowed:

(1) To a holding company affiliate of a bank, as defined in section 2 of the Banking Act of 1933 (12 U.S.C. 221a), which holding company affiliate holds, at the end of the taxable year, a general voting permit granted by the Board of Governors of the Federal Reserve System.

(2) In the amount of the earnings or profits of such holding company affiliate which, in compliance with section 5144 of the Revised Statutes (12 U.S.C. 61), has been devoted by it during the taxable year to the acquisition of readily marketable assets other than bank stock.

(3) Upon certification by the Board of Governors of the Federal Reserve System to the Commissioner that such an amount of the earnings or profits has been so devoted by such affiliate during the taxable year.

No deduction is allowable under section 601 for the amount of readily marketable assets in excess of what is required by section 5144 of the Revised Statutes (12 U.S.C. 61) to be acquired by such affiliate, or in excess of the taxable income for the taxable year computed without regard to the special deductions for corporations provided in part VIII (section 241 and following), subchapter B, chapter 1 of the Code. Nor may the aggregate of the deductions allowable under section 601 and the credits allowable under the corresponding provision of any prior income tax law for all taxable years exceed the amount required to be devoted under such section 5144 to the acquisition of readily marketable assets other than bank stock.

(b) Every taxpayer claiming a deduction provided for in section 601 shall attach to its return a supplementary statement setting forth all the facts and information upon which the claim

is predicated, including such facts and information as the Board of Governors of the Federal Reserve System may prescribe as necessary to enable it, upon the request of the Commissioner subsequent to the filing of the return, to certify to the Commissioner the amount of earnings or profits devoted to the acquisition of such readily marketable assets. A certified copy of such supplementary statement shall be forwarded by the taxpayer to the Board of Governors at the time of the filing of the return. The holding company affiliate shall also furnish the Board of Governors such further information as the Board shall require. For the requirements with respect to the amount of such readily marketable assets which must be acquired and maintained by a holding company affiliate to which a voting permit has been granted, see section 5144(b) and (c) of the Revised Statutes (12 U.S.C. 61).

NATURAL RESOURCES

DEDUCTIONS

§ 1.611–0 Regulatory authority.

Sections 1.611–1 through 1.614–8, inclusive, are prescribed under the authority granted the Secretary or his delegate by section 611(a) of the Code to prescribe regulations under which a reasonable allowance for depletion and depreciation of improvements shall be allowed, according to the peculiar conditions in each case, in the case of mines, oil and gas wells, other natural deposits and timber.

[T.D. 6965, 33 FR 10692, July 26, 1968]

§ 1.611–1 Allowance of deduction for depletion.

(a) *Depletion of mines, oil and gas wells, other natural deposits, and timber*—(1) *In general.* Section 611 provides that there shall be allowed as a deduction in computing taxable income in the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion. In the case of standing timber, the depletion allowance shall be computed solely upon the adjusted basis of the property. In the case of other exhaustible natural resources the allowance for depletion shall be computed upon either the adjusted depletion basis of the property (see section 612, relating to cost depletion) or upon a percentage of gross income from the property (see section 613, relating to percentage depletion), whichever results in the greater allowance for depletion for any taxable year. In no case will depletion based upon discovery value be allowed.

(2) See § 1.611–5 for methods of depreciation relating to improvements connected with mineral or timber properties.

(3) See paragraph (d) of this section for definition of terms.

(b) *Economic interest.* (1) Annual depletion deductions are allowed only to the owner of an economic interest in mineral deposits or standing timber. An economic interest is possessed in every case in which the taxpayer has acquired by investment any interest in mineral in place or standing timber and secures, by any form of legal relationship, income derived from the extraction of the mineral or severance of the timber, to which he must look for a return of his capital. For an exception in the case of certain mineral production payments, see section 636 and the regulations thereunder. A person who has no capital investment in the mineral deposit or standing timber does not possess an economic interest merely because through a contractual relation he possesses a mere economic or pecuniary advantage derived from production. For example, an agreement between the owner of an economic interest and another entitling the latter to purchase or process the product upon production or entitling the latter to compensation for extraction or cutting does not convey a depletable economic interest. Further, depletion deductions with respect to an economic interest of a corporation are allowed to the corporation and not to its shareholders.

(2) No depletion deduction shall be allowed the owner with respect to any timber, coal, or domestic iron ore that such owner has disposed of under any form of contract by virtue of which he retains an economic interest in such timber, coal, or iron ore, if such disposal is considered a sale of timber, coal, or domestic iron ore under section 631 (b) or (c).